



JOHN CHIANG
California State Controller

September 17, 2008

K-12 Local Education Agencies, Charter Schools,
Sponsoring Charter Entities, Joint Powers Entities, and
Certified Public Accountants Performing Audits of K-12 Local
Education Agencies, Charter Schools, and Joint Powers Entities

Re: Annual Audits for Fiscal Year 2007-08

This advisory provides information to assist independent auditors in performing the fiscal year 2007-08 audits of Local Education Agencies (LEAs), charter schools, and joint powers entities.

Procedural

1. The requirements specified in *Education Code* 41020 are applicable to all LEAs, including joint power entities and charter schools. As a result, audits shall be conducted in accordance with auditing standards generally accepted in the United States of America, the standards set forth in *Government Auditing Standards* issued by the Comptroller General of the United States, and the provisions of *California Code of Regulations* (CCR), Title 5, Education, Section 19810, et seq.
2. The report shall be presented as prescribed in the *Standards and Procedures for Audits of California K-12 Local Educational Agencies 2007-08*. For additional guidance, refer to the American Institute of Certified Public Accountants (AICPA) *Audit and Accounting Guide for State and Local Governments* and the AICPA *Government Auditing Standards and Circular A-133 Audits* with conforming changes as of May 1, 2008.
3. Charter schools that are included in the sponsoring entity's financial statement audit are not required to submit a separate report to the State Controller's Office (SCO), the California Department of Education (CDE), or the local County Office of Education.
4. For audits where charter schools are included in the district's financial statement audit, the auditor is expected to stratify the sample so that a representative number of charter schools (classroom and non-classroom based) are tested annually for state compliance and federal compliance, if applicable. In cases where a district has only one charter school, the auditor must apply state compliance audit procedures annually.
5. The State's report certification process requires that the SCO perform a desk review of the LEA's annual audit report. The review will ensure that the audit report meets the minimum reporting standards contained in the audit guide. The SCO will then reject or certify the report.

If the SCO rejects the report, a letter is sent to the independent auditor and LEA that describes the exception(s) noted during the SCO's review. The auditor has 30 days from receipt of the letter to make the correction. Upon receipt, the SCO will review the revised audit report and notify the auditor and LEA of the review results. The audit fee percentage stipulated in the audit contract must be withheld until the audit report is certified.

If the SCO certifies the report, the LEA and auditor will receive a letter stating that the audit report conforms to the reporting standards contained in the audit guide. The letter also specifies that the LEA may release the portion of the audit fee withheld under the provisions of *California Education Code* Section 14505.

If the audit report contains a finding or findings that may be considered apportionment significant, the LEA receives a certification letter with information on its appeal rights. The LEA has 30 days, from the date the U.S. Postal Service delivers the letter, to request summary review of any apportionment significant audit finding or findings, on the grounds of substantial compliance. In addition, the LEA has 60 days from delivery of the letter or 30 days following the conclusion of a summary review, with regard to the findings included in that review, to file a formal appeal of any apportionment significant finding or findings on any one or more of the grounds set forth in California Education Code section 41344(d). For more information on audit finding appeals, visit the Education Audit Appeals Panel Website at <http://eaap.ca.gov/NewWebSite0804/EAAPAppeals.htm>.

6. Fiscal year 2007-08 audit reports must be filed with the SCO, CDE, local County Superintendent of Schools, and, if applicable, the chartering entity, by December 15, 2008. Independent auditors may submit the SCO's copy of the report either by mail or via File Transfer Protocol (FTP).

To request FTP instructions, submit your request to the Education Oversight unit at leaaudits@sco.ca.gov. Please indicate if you are requesting FTP instructions with or without Username and Password information. Instructions containing Username and Password information will be mailed to the address on file. Instructions without Username and Password information will be e-mailed.

Mailing Address

State Controller's Office
Division of Audits
School District Audits
Post Office Box 942850
Sacramento, CA 94250-5874

Private Carrier Delivery

State Controller's Office
Division of Audits
School District Audits
300 Capitol Mall, Fourth Floor
Sacramento, CA 95814

7. The County Office of Education must submit a report extension request to the SCO and the CDE by December 1, 2008. The extension request must come from the County Office of Education and not the LEA. The SCO will not consent to the extension request unless the circumstance leading to the extension is extraordinary.

The SCO does not grant extensions for charter school audits. The extension must be obtained through the chartering entity, and the chartering entity should notify the SCO and the CDE of the extension.

8. Certified public accountants or public accountants wanting to conduct LEA audits must be added to the Certified Public Accountants Directory published by the SCO. To be included in the directory, a written request must be submitted to the SCO prior to conducting the audits. Instructions for submitting the request can be found at the SCO's website <http://www.sco.ca.gov/cpads/main/default.aspx>.
9. The auditor-rotation requirements specified in *California Education Code* Section 41020 (f)(2) apply to auditors who conduct LEA audits. This section of the *Education Code* makes it unlawful for a public accounting firm to provide audit services to the LEA if the lead audit partner, or coordinating audit partner responsible for the audit or for reviewing the audit, has performed audit services for the LEA in each of the six previous fiscal years. Consequently a different audit firm and/or audit partners must be used in the seventh year, unless a waiver is obtained from the Education Audit Appeals Panel.
10. To obtain a copy of the Desk Review Checklist for K-12 LEAs or obtain the status of an LEA audit report, you may send a request to leaaudits@sco.ca.gov or leave a voicemail message at (916) 324-6442.

Audit Guide

The audit guide is published by the Education Audit Appeals Panel (EAAP) pursuant to rulemaking procedures. The title of the audit guide for fiscal year 2007-08 is *Standards and Procedures for Audits of California K-12 Local Educational Agencies 2007-08*. The audit guide is prescribed in 5 CCR, section 19810, et seq. It is available through the EAAP's Web site at www.eaap.ca.gov.

Note that 5 CCR, section 19816.1 (a)(5), erroneously omitted sections 19833.5 and 19833.6. These sections are applicable to fiscal year 2007-08 and should be audited.

Compliance

During the SCO's annual audit report certification process, a significant amount of time is spent corresponding with independent auditors regarding audit report deficiencies. To expedite certification of audit reports for fiscal year 2007-08, the SCO requests that auditors attend to the following when completing their audit reports.

1. The Auditor's Report on State Compliance must refer to *Standards and Procedures for Audits of California K-12 Local Educational Agencies 2007-08*, published by the Education Audit Appeals Panel.
2. The Auditor's Report on State Compliance must identify the state compliance requirements specified in Section 19816 (f)(5) of the *Standards and Procedures for Audits of California K-12 Local Educational Agencies 2007-08*. The report must include the number of procedures required by the audit guide and state whether or not the procedures were performed. An explanation must be included if certain procedures were not performed or if alternate procedures were performed.

3. The following compliance requirements were added to the audit guide for fiscal year 2007-08.

LEAs other than Charter Schools:

- Section 19829.5, Classroom Teacher Salaries, one procedure
- Section 19838, Mathematics and Reading Professional Development, four procedures

School Districts and Charter Schools:

- Section 19846, After School Education and Safety Program, general requirements four procedures; after school four procedures; before school five procedures

Charter Schools:

- For charter schools, the “Schedule of Daily Attendance” must include total Average Daily Attendance and Average Daily Attendance generated through classroom-based instruction (section 19816(h)).
4. When determining if the minimum percentage requirements were met regarding Classroom Teacher Salaries (per section 19829.5, “the percent of current cost of education expended for classroom compensation”), do not round beyond the one hundredth percent. For example, 59.85% should not be rounded to 60.00%.
 5. Each audit finding should be presented in the following level of detail:
 - State or Federal Program Information
 - Finding Code (e.g., 10000 Attendance, 20000 Inventory of Equipment)
 - Criteria or specific requirement
 - Condition
 - Effect
 - Cause
 - Questioned costs
 - Recommendation
 - LEA’s corrective action plan
 6. For state compliance findings, the financial impact must be quantified. The audit guide includes specific information that must be included in each finding. This information must be presented in order for the SCO to accept the finding. For example, for attendance findings, the audit guide requires that the audit report include a statement of the number of units of average daily attendance that were inappropriately reported for apportionment and an estimate of their dollar value. If there is no financial impact, the finding must describe the reasons for the auditor’s conclusion.
 7. For state compliance findings, the stated criteria should refer to a California state law or regulation that governs the program. The SCO will not accept reports which cite the *Standards and Procedures for Audits of California K-12 Local Educational Agencies 2007-08* as the criteria.

8. For single audits with federal compliance findings, the SCO will not accept reports in which federal findings are not presented in accordance with the Office of Management and Budget (OMB) Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, subpart E–Auditors, section .510.
9. LEAs are required by Federal regulation to calculate and remit interest earned on federal cash advances on a timely basis. For single audits, Code of Federal Regulations (CFR), Title 34, Education, Part 80, Uniform Administrative Requirements for Grants and Cooperative Agreements to State and Local Governments, subpart C-Post-Award Requirements Financial Administration, section 80.21(i) states “except for interest earned on advances of funds exempt under the Intergovernmental Cooperation Act and the Indian Self-Determination Act, grantees and subgrantees shall promptly, but at least quarterly, remit interest earned on advances to the Federal agency. The grantee or subgrantee may keep interest amounts up to \$100 per year for administrative expenses.”

OMB’s A-133 Compliance Supplement addresses the interest requirement contained in 34 CFR 80.21(i). Part 3-Compliance Requirements, section C-Cash Management, states that interest earned on advances by local government grantees and subgrantees is required to be submitted promptly, but at least quarterly, to the Federal agency. Audit Objective 5 directs auditors to “determine whether interest earned on advances was reported/remitted as required.” The Suggested Audit Procedures – Compliance for Other Recipients and Subrecipients (which would encompass LEAs), step 10, suggests that auditors “review records to determine if interest was earned on Federal cash draws. If so, review evidence to ascertain whether it was returned to the appropriate agency.”

Auditors may want to consider assessing LEA compliance with the interest requirement across all Federal programs. The Compliance Supplement states “the procedures are intended to be applied to each program determined to be major. However, due to the nature of cash management and the system of cash management in place in a particular entity, it may be appropriate and more efficient to perform these procedures for all programs collectively rather than separately for each program.”

10. Updated Report Format: The Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with Government Auditing Standards, and the Report on Compliance with Requirements Applicable to Each Major Program and on Internal Control Over Compliance in Accordance with OMB Circular A-133 must be updated in accordance with Statement on Auditing Standards (SAS) No. 112, Communicating Internal Control Related Matters Identified in an Audit. SAS 112 is effective for audits of financial statements for periods ending on or after December 15, 2006.
11. Management Letter: A copy of the management letter, if issued, must be submitted along with the LEA’s annual report.

This audit guide advisory is available on the Internet, at <http://www.sco.ca.gov/pubs/index.shtml#guides>.

Should you have any questions or need additional information, please contact Casandra Moore-Hudnall, Chief, Financial Audits Bureau, Division of Audits, at (916) 322-4846.

Sincerely,

Original signed by

MICHAEL CARTER
Chief Operating Officer
State Controller's Office

MC/sk

7019

cc: Jack O'Connell
Superintendent
California Department of Education